# LEGISLATIVE SERVICES AGENCY
## OFFICE OF FISCAL AND MANAGEMENT ANALYSIS

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## FISCAL IMPACT STATEMENT

**LS 6766** **NOTE PREPARED:** Jan 24, 2005
**BILL NUMBER:** HB 1756 **BILL AMENDED:**

**SUBJECT:** Income Tax Exemption for Pension Income.

**FIRST AUTHOR:** Rep. Whetstone **BILL STATUS:** As Introduced
**FIRST SPONSOR:**

**FUNDS AFFECTED:** X **GENERAL** **IMPACT:** State & Local
X **DEDICATED**
**FEDERAL**

**Summary of Legislation:** The bill exempts income from pensions, annuities, and individual retirement accounts (IRAs) from Adjusted Gross Income Taxation. The bill makes conforming amendments to existing provisions that provide certain partial deductions for retirement income and also makes a technical correction. The bill also repeals a provision that provides a partial deduction for Federal Civil Service Annuity Income.

**Effective Date:** January 1, 2006.

**Explanation of State Expenditures:** The Department of State Revenue (DOR) would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to incorporate this deduction. The DOR's current level of resources should be sufficient to implement these changes.

**Explanation of State Revenues:** The bill would reduce state Adjusted Gross Income (AGI) Tax liabilities of individual taxpayers who receive IRA distributions or pension or annuity income. The revenue loss due to this bill could potentially total $413.0 M in FY 2007, growing thereafter by approximately 9% to 9.5% annually.

*Background:* The bill allows a taxpayer to deduct pension and annuity income and taxable IRA distributions from AGI beginning in tax year 2006. The bill does not limit the amount that a taxpayer may deduct. The fiscal impact estimate is based on federal income tax data from 1990 to 2002 for taxable pension/annuity distributions; and from 1996 to 2002 for taxable IRA distributions. The data for tax year 2002 indicates that 532,849 Indiana residents reported taxable pension or annuity income totaling about $6,721.0 M. In addition, 197,020 Indiana residents reported taxable IRA distributions totaling about $1,956.4 M. The 2002 data is used as the base to project pension and annuity and IRA distribution totals for tax years 2003 and after. The projections rely on recent annual growth rates for these reported income totals. In addition, the fiscal impact is a net total after subtraction of currently deducted civil service annuity and military pension income. Under current statute up to $2,000 in civil service or military retirement is allowed to be deducted from AGI. The 2002 state deduction amounts are used as the base for projections in 2003 and after. These projections are based on recent annual growth rates in these two series.

Since the deduction is effective beginning in tax year 2006, the fiscal impact would begin in FY 2007. Eighty-six percent of the revenue from the AGI Tax on individuals is deposited in the state General Fund, and 14% of this revenue is deposited in the Property Tax Replacement Fund.

**Explanation of Local Expenditures:**

**Explanation of Local Revenues:** Because the proposed deduction would serve to decrease taxable income, counties imposing local option income taxes (CAGIT, COIT, and/or CEDIT) may, as a result, experience a significant decrease in revenue from these taxes.

**State Agencies Affected:** Department of State Revenue.

**Local Agencies Affected:** Counties with local option income taxes.

**Information Sources:** Internal Revenue Service, Statistics on Income; OFMA income tax databases: 1990-2002. OFMA Income Tax databases, 1996-2002.

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